Tennessee Board of Regents
Middle Tennessee State University

For the Year Ended
June 30, 2003

Arthur A. Hayes, Jr., CPA, JD, CFE
Director

Charles K. Bridges, CPA
Assistant Director

Shirley A. Henry, CPA
Audit Manager

James Ligon
In-Charge Auditor

Keith Isbell
Barbara Ragan, CFE
Iffath Sajid
Staff Auditors

Gerry Boaz, CPA
Technical Analyst

Amy Brack
Editor

Comptroller of the Treasury, Division of State Audit
1500 James K. Polk Building, Nashville, TN 37243-0264
(615) 401-7897

Financial/compliance audits of colleges and universities are available on-line at
www.comptroller.state.tn.us/sa/reports/index.html.
For more information about the Comptroller of the Treasury, please visit our Web site at
www.comptroller.state.tn.us.

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
State Capitol
Nashville, Tennessee 37243-0260
(615) 741-2501

John G. Morgan
Comptroller

March 30, 2004

The Honorable Phil Bredesen, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
The Honorable Charles W. Manning, Chancellor
Tennessee Board of Regents
1415 Murfreesboro Road, Suite 350
Nashville, Tennessee 37217
and
Dr. Sidney A. McPhee, President
Middle Tennessee State University
110 Cope Administration Building
Murfreesboro, Tennessee 37132

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Board of Regents, Middle Tennessee State University, for the year ended June 30, 2003. You will note from the independent auditor's report that an unqualified opinion was given on the fairness of the presentation of the financial statements.

Consideration of internal control over financial reporting and tests of compliance resulted in no audit findings.

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/th
04/010

State of Tennessee

Audit Highlights

Comptroller of the Treasury — Division of State Audit

Financial and Compliance Audit
Middle Tennessee State University
For the Year Ended June 30, 2003

AUDIT OBJECTIVES

The objectives of the audit were to consider the university's internal control over financial reporting; to determine compliance with certain provisions of laws, regulations, contracts, and grants; to determine the fairness of the presentation of the financial statements; and to recommend appropriate actions to correct any deficiencies.

AUDIT FINDINGS

The audit report contains no findings.

OPINION ON THE FINANCIAL STATEMENTS

The opinion on the financial statements is unqualified.

Audit Report
Tennessee Board of Regents
Middle Tennessee State University
For the Year Ended June 30, 2003

TABLE OF CONTENTS

TABLE OF CONTENTS (CONT.)

Tennessee Board of Regents
Middle Tennessee State University
For the Year Ended June 30, 2003

INTRODUCTION

POST-AUDIT AUTHORITY

This is a report on the financial and compliance audit of the Tennessee Board of Regents, Middle Tennessee State University. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated,* which authorizes the Department of Audit to "perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller."

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

Middle Tennessee State University was first established in 1911 as Middle Tennessee State Normal School in Murfreesboro, Tennessee. In 1925, when the General Asembly provided for three teachers' colleges—one in each of the grand divisions—Middle Tennessee State Normal School became Middle Tennessee State Teachers' College and gained the power to grant the Bachelor of Science degree. The college's name was changed to Middle Tennessee State College by an act of the legislature in 1943 and to Middle Tennessee State University by a special legislative act in 1956. The university is composed of the Graduate School, the Office of Continuing Studies and Public Service, and five undergraduate colleges: Basic and Applied Sciences, Business, Education, Liberal Arts, and Mass Communications.

ORGANIZATION

The governance of Middle Tennessee State University is vested in the Tennessee Board of Regents. The Governor, the Commissioner of Education, the Commissioner of Agriculture, and the Director of the Tennessee Higher Education Commission serve *ex officio* on this board. The chief administrative officer of the university is the president, who is assisted and advised by members of the faculty and administrative staff.

AUDIT SCOPE

The audit was limited to the period July 1, 2002, through June 30, 2003, and was conducted in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Financial statements are presented for the year ended June 30, 2003, and for comparative purposes, the year ended June 30, 2002. Middle Tennessee State University is an institution of the Tennessee Board of Regents, which is an integral part of state government. As such, the Tennessee Board of Regents has been included as a component unit in the *Tennessee Comprehensive Annual Financial Report.*

OBJECTIVES OF THE AUDIT

The objectives of the audit were

1. to consider the university's internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements;
2. to determine compliance with certain provisions of laws, regulations, contracts, and grants;
3. to determine the fairness of the presentation of the financial statements; and
4. to recommend appropriate actions to correct any deficiencies.

Although this audit was not intended to serve as an organization-wide audit as described in the Single Audit Act, as amended by the Single Audit Act Amendments of 1996, and Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, it included tests of compliance with applicable federal laws and regulations and consideration of internal control used in administering federal financial assistance programs. This audit is a segment of the organization-wide audit of the State of Tennessee, which is conducted in accordance with the Single Audit Act.

PRIOR AUDIT FINDINGS

There were no findings in the prior audit report.

OBSERVATIONS AND COMMENTS

The university is the sole beneficiary of the Middle Tennessee State University Foundation, which is a private, nonprofit foundation. The foundation's accounts are in the agency funds of the university. We reviewed limited areas of the foundation's activities and discussed the activities with pertinent university and foundation officials, and nothing came to our attention in those limited areas that indicated there were any problems related to the foundation.

RESULTS OF THE AUDIT

AUDIT CONCLUSIONS

Internal Control

As part of the audit of the university's financial statements for the year ended June 30, 2003, we considered internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements, as required by auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Consideration of internal control over financial reporting disclosed no material weaknesses.

Compliance

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Fairness of Financial Statement Presentation

The Division of State Audit has rendered an unqualified opinion on the university's financial statements.

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-0264
PHONE (615) 401-7897
FAX (615) 532-2765

Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

November 20, 2003

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the financial statements of Middle Tennessee State University, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, as of and for the year ended June 30, 2003, and have issued our report thereon dated November 20, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

<u>Compliance</u>

As part of obtaining reasonable assurance about whether the university's financial statements are free of material misstatement, we performed tests of the university's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

We did, however, note one less significant instance of noncompliance, which we have reported to the university's management in a separate letter.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the university's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a conditon in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that mistatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performinng their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weakness.

However, we noted certain matters involving the internal control over financial reporting, which we have reported to the university's management in a separate letter.

This report is intended solely for the information and use of General Assembly of the State of Tennessee and management and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record.

Sincerely,

Arthur A. Hayes, Jr., CPA,
Director

AAH/th

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-0264
PHONE (615) 401-7897
FAX (615) 532-2765

Independent Auditor's Report

November 20, 2003

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the accompanying statements of net assets of Middle Tennessee State University, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, as of June 30, 2003, and June 30, 2002, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the university's management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Tennessee Board of Regents, Middle Tennessee State University, as of June 30, 2003, and June 30, 2002, and the revenues, expenses, and changes in net assets and the cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Honorable John G. Morgan
November 20, 2003
Page Two

As discussed in Note 12, during the year ended June 30, 2002, the university implemented GASB Statement 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, and GASB Statement 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*. The university also implemented GASB Statement 37, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments: Omnibus*, and GASB Statement 38, *Certain Financial Statement Note Disclosures*.

The management's discussion and analysis on pages 8 through 20 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 20, 2003, on our consideration of the university's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

Arthur A. Hayes, Jr.

Arthur A. Hayes, Jr., CPA,
Director

AAH/th

MIDDLE TENNESSEE STATE UNIVERSITY
Management's Discussion and Analysis
For the Year Ended June 30, 2003

This section of Middle Tennessee State University's annual financial report presents a discussion and analysis of the financial performance of the university during the fiscal year ended June 30, 2003, with comparative information presented for the fiscal year ended June 30, 2002. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the financial statements and notes. The financial statements, notes, and this discussion are the responsibility of management.

Using This Annual Report

This report consists of three basic financial statements. The Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows provide information on Middle Tennessee State University as a whole and present a long-term view of the university's finances.

The Statement of Net Assets

The Statement of Net Assets presents the financial position of the university at the end of the fiscal year and includes all assets and liabilities of the university. The difference between total assets and total liabilities—net assets—is an indicator of the current financial condition of the university. Assets and liabilities are generally measured using current values. One notable exception is capital assets, which are stated at historical cost less an allowance for depreciation.

Net assets are divided into three major categories. The first category, invested in capital assets, net of related debt, provides the university's equity in property, plant, and equipment owned by the university. The next asset category is restricted net assets, which is divided into two categories, nonexpendable and expendable. The corpus of nonexpendable restricted resources is only available for investment purposes. Expendable restricted net assets are available for expenditure by the university but must be spent for purposes as determined by donors and/or external entities that have placed time or purpose restrictions on the use of the assets. The final category is unrestricted net assets. Unrestricted net assets are available to the institution for any lawful purpose of the institution.

Statement of Net Assets
(in thousands of dollars)

	2003	2002
Assets :		
Current assets	$ 70,062	$ 65,612
Capital assets, net	191,363	182,612
Other assets	25,843	27,298
Total assets	**287,268**	**275,522**

Liabilities:		
Current liabilities	75,210	69,340
Noncurrent liabilities	84,878	80,875
Total liabilities	**160,088**	**150,215**
Net assets :		
Invested in capital assets, net of related debt	89,235	87,837
Restricted – nonexpendable	716	626
Restricted – expendable	5,585	6,871
Unrestricted	31,643	29,973
Total net assets	**$ 127,179**	**$ 125,307**

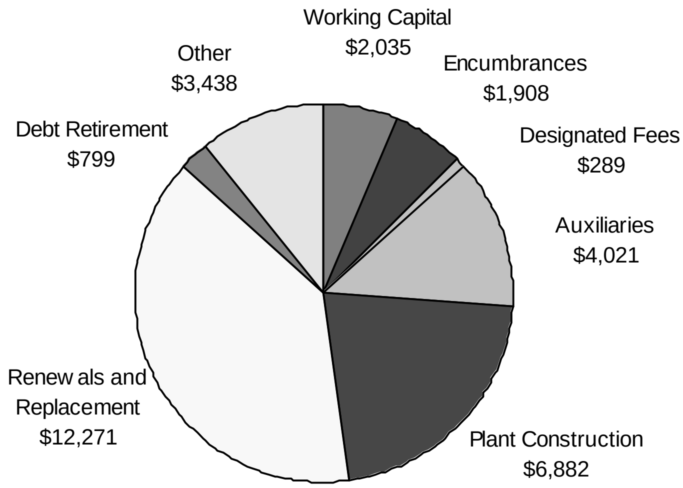
- Current assets increased by $4,450,172. This increase is partially due to a significant increase in the short-term investments category, which is the result of donations to the MTSU Foundation.

- Current liabilities increased by $5,870,318. This increase in current liabilities is primarily the result of an increase in the deposits held in custody for others category. The increase is attributed to the construction of the Tennessee Miller Coliseum by the MTSU Foundation, along with additions of current year donations.

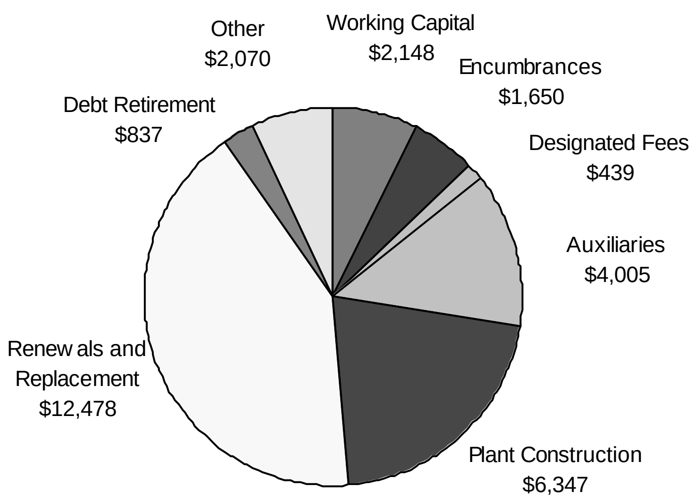
- Noncurrent liabilities increased by $4,003,031. The most significant cause for the increase was the issuance of commercial paper by the Tennessee State School Bond Authority on behalf of the university for the following projects: purchase of Steinway pianos for the School of Music, purchase of a new fleet of airplanes for the Aerospace Department, property acquisitions around the perimeter of the campus, and renovation of the Smith Hall Complex for student housing.

Many of the university's unrestricted net assets have been designated or reserved for specific purposes such as: repairs and replacement of equipment, future debt service, quasi-endowments, and capital projects. The following graphs show the allocations (in thousands of dollars):

Allocations of Unrestricted Net Assets 2003



Allocations of Unrestricted Net Assets 2002



- Plant construction increased by $534,855. This is the result of increases in various capital project balances, which are funded by both appropriations and local funds, netted with decreases in other capital project balances.

- The other category increased by $1,368,818. Contributing factors to this increase are an increase in the allocation for the 2003-04 budget and an increase in the unrestricted net assets.

The Statement of Revenues, Expenses, and Changes in Net Assets

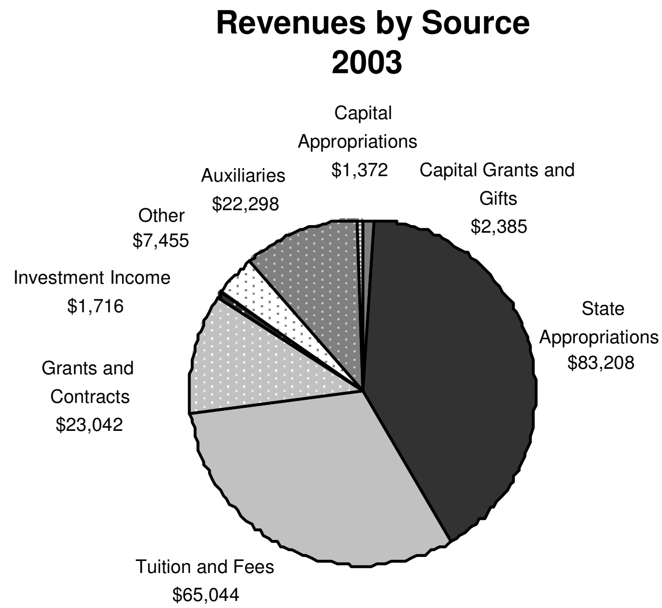
The Statement of Revenues, Expenses, and Changes in Net Assets presents the operating results of the university, as well as the nonoperating revenues and expenses. Annual state appropriations, while budgeted for operations, are considered nonoperating revenues according to generally accepted accounting principles.

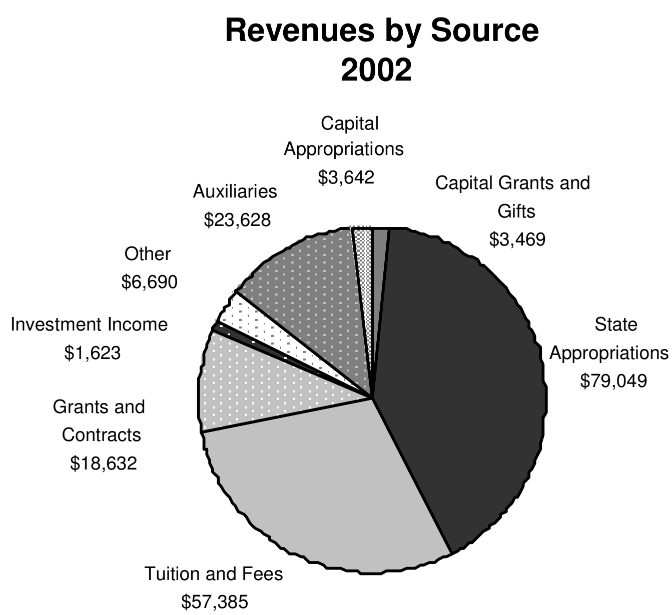
Statement of Revenues, Expenses, and Changes in Net Assets
(in thousands of dollars)

	2003	2002
Operating revenues:		
Net tuition and fees	$ 65,044	$ 57,385
Grants and contracts	23,042	18,632
Auxiliaries	22,298	23,628
Other	5,956	4,975
Total operating revenues	**116,340**	**104,620**
Operating expenses	200,429	189,583
Operating loss	**(84,089)**	**(84,963)**
Nonoperating revenues and expenses:		
State appropriations	83,208	79,049
Gifts	929	901
Investment income	1,716	1,623
Other revenues and expenses	(3,597)	(3,112)
Total nonoperating revenues and expenses	**82,256**	**78,461**
Loss before other revenues, expenses, gains, or losses	**(1,833)**	**(6,502)**
Other revenues, expenses, gains, or losses:		
Capital appropriations	1,372	3,642
Capital grants and gifts	2,385	3,469
Other	(52)	-
Total other revenues, expenses, gains, or losses	**3,705**	**7,111**
Increase in net assets	**1,872**	**609**
Net assets at beginning of year, as originally reported	125,307	256,373
Cumulative effect of changes in accounting principle	-	(131,675)
Net assets at beginning of year, as restated	**125,307**	**124,698**
Net assets at end of year	**$ 127,179**	**$ 125,307**

Revenues

The following is a graphic illustration of revenues by source (both operating and nonoperating), which were used to fund the university's operating activities for the years ended June 30, 2003, and June 30, 2002 (in thousands of dollars).





- Tuition and fees increased by $7,658,425. Student enrollment increased approximately 5% from fall 2001 to fall 2002. Across the board fee increases were approved for 2002-03 by the Tennessee Board of Regents, thus increasing student fees by 8%.

- Grants and contracts increased by $4,409,153. This increase was due to an increase in the university's Pell Grant award of approximately $1,800,000, significant increases in existing grant program revenues, and the addition of several new grant programs.

- Capital appropriations decreased by $2,270,184. This decrease in capital appropriations was the result of fewer capital projects being approved by the Tennessee State Building Commission for 2002-03.

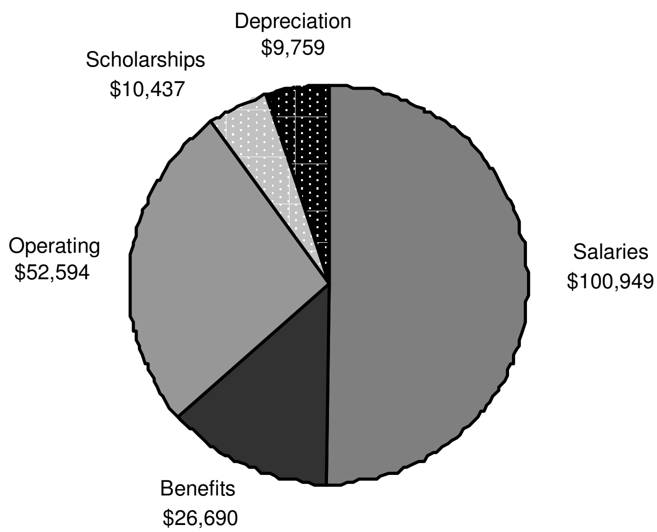
Expenses

Operating expenses can be displayed in two formats, natural classification and program classification. Both formats are displayed below in thousands of dollars.

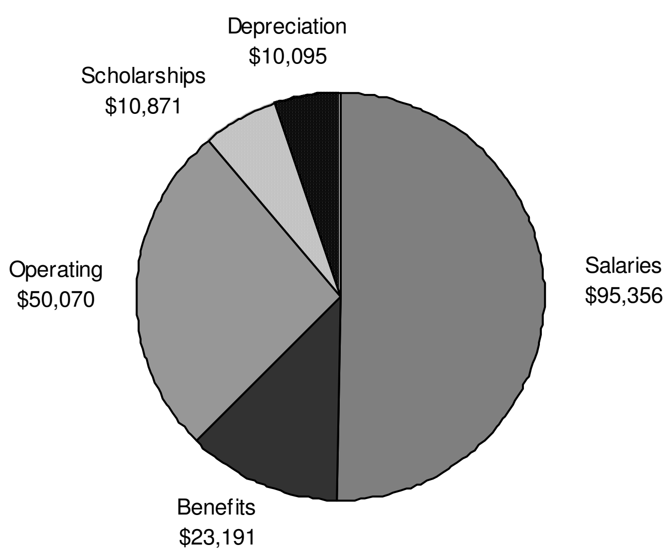
Natural Classification
(in thousands of dollars)

	2003	**2002**
Salaries	$ 100,949	$ 95,356
Benefits	26,690	23,191
Operating	52,594	50,070
Scholarships	10,437	10,871
Depreciation	9,759	10,095
Total	$ 200,429	$ 189,583

Expenses by Program Classification
2003



Expenses by Program Classification
2002



- Salaries increased by $5,592,235. This increase in salary expenses is primarily due to salary increases given to employees in January 2002 (2% for faculty and 1% for administrative and classified) and January 2003 (5% for faculty and 4% for administrative and classified). Other factors contributing to this increase are faculty promotions, new faculty positions, and new Public Safety officer positions.

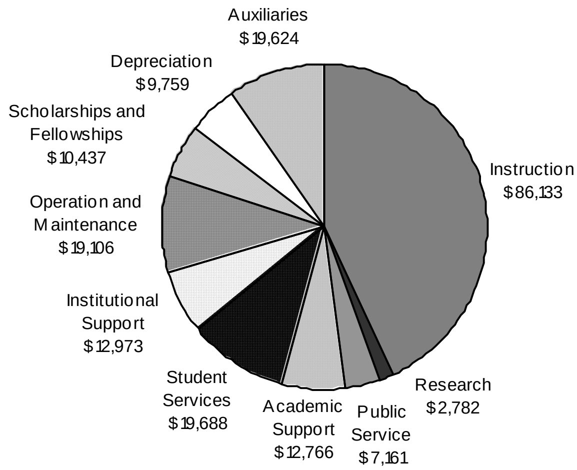
- Benefits increased by $3,498,740. The increase is due to increases in the state's group insurance premiums in January 2002 and January 2003, increase in TCRS rates, and added benefits for new positions.

Program Classification

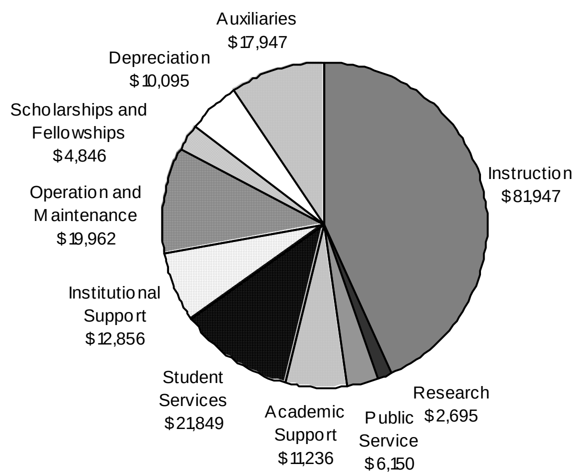
(in thousands of dollars)

	2003	2002
Instruction	$ 86,133	$ 81,947
Research	2,782	2,695
Public service	7,161	6,150
Academic support	12,766	11,236
Student services	19,688	21,849
Institutional support	12,973	12,856
Operation and maintenance	19,106	19,962
Scholarships and fellowships	10,437	4,846
Auxiliaries	19,624	17,947
Depreciation	9,759	10,095
Total	$ 200,429	$ 189,583

Expenses by Program Classification
2003



Expenses by Program Classification
2002



- The instruction function increased by $4,185,885. This increase is primarily the result of faculty salary increases in January 2002 and January 2003, faculty promotions, and new faculty positions.

- The scholarship function increased by $5,591,145. Starting in 2002-03, all scholarship expenses are shown in the scholarship function rather than reporting them as part of each function. The result of this reporting is a significant increase in expenses in the scholarship function for 2002-03.

The Statement of Cash Flows

The Statement of Cash Flows provides information about cash receipts and cash payments during the year. This statement also assists users in assessing the university's ability to generate net cash flows, its ability to meet its obligations as they come due, and its need for external financing.

Statement of Cash Flows
(in thousands of dollars)

	2003	2002
Cash provided (used) by:		
Operating activities	$ (72,668)	$ (70,056)
Noncapital financing activities	83,469	77,653
Capital and related financing activities	(11,659)	(5,967)
Investing activities	1,684	1,666
Net increase in cash	**826**	**3,296**
Cash, beginning of year	**58,901**	**55,605**
Cash, end of year	**$ 59,727**	**$ 58,901**

- In the noncapital financing activities section of the Statement of Cash Flows, state appropriations increased by $5,330,100 over the previous year.

- In the capital and related financing activities section, capital appropriations decreased by $2,270,184. Capital grants and gifts received also decreased by $3,260,352, which was primarily the result of gifts received in 2001-02 for the construction of the Paul W. Martin, Sr. Hall to house the Honors College.

- The university’s cash position for the year increased by $825,960.

Capital Assets and Debt Administration

Capital Assets

At June 30, 2003, Middle Tennessee State University had $170,627,179 invested in capital assets, net of accumulated depreciation of $113,865,683. Depreciation charges totaled $9,758,808 for the current fiscal year. Details of these assets are shown below.

Schedule of University Capital Assets, Net of Depreciation
(in thousands of dollars)

	2003	2002
Land	$ 4,527	$ 4,449
Land improvements and infrastructure	13,195	14,142
Buildings	124,449	128,186
Equipment	12,438	9,182
Library holdings	8,323	7,851
Projects in progress	7,695	1,891
Total	$ 170,627	$ 165,701

Some highlights of the information presented on the Schedule of University Capital Assets, Net of Depreciation are as follows

- ♦ Buildings decreased by $3,736,813. This decrease is the result of the recording of the current year building depreciation of $4,852,010 and the completion of only one building. The Development Facility in the amount of $1,146,773 was transferred in from projects in progress.
- ♦ Equipment increased by $3,255,955 primarily from the purchase of Steinway pianos in the amount of $1,226,646 from donated funds to the School of Music and the purchase of a new fleet of airplanes for the Aerospace Department totaling $1,987,024 for the fiscal year.
- ♦ Projects in progress increased by $5,803,909. Major projects under construction during the year included the construction of the Paul W. Martin, Sr. Hall to house the Honors College, construction of a pad to mount a donated 727 jet, improvements to several parking areas throughout campus, renovations to several housing facilities, renovations to the Keathley University Center, and the planning phase for the renovation of the Todd Building.

The following projects will be underway during the next fiscal year:

- ♦ The Todd Building, formerly the Todd Library, is currently being renovated to house the Art Department and the Gore Center. The project will be substantially complete at the beginning of fiscal year 2004-05. The total project cost is $9,355,000, which is funded by state capital funds.
- ♦ The university housing facilities are in the initial phases of a 10-year renovation plan, which includes major renovation of most of the housing facilities. Renovation plans for fiscal year 2003-04 include major renovations of Beasley, Sims, Judd and Gracy, and other minor renovations in Family Housing, Rutledge, and Monohan. These renovation projects are funded through TSSBA bond funds supported by housing auxiliary fees.
- ♦ The Paul W. Martin, Sr. Hall, a 19,000 gross square feet building to house the Honors College, is currently under construction. Substantial completion is expected during fiscal year 2003-04, and is funded through a $2,000,000 gift by Paul W. Martin, Jr. and Lee Martin, and matching gift funds by other generous donors.

At June 30, 2003, the Middle Tennessee State University Foundation had $20,735,167 invested in capital assets, net of accumulated depreciation of $452,512. Depreciation charges totaled $438,860 for the current fiscal year. Details of these assets are shown below.

Schedule of Foundation Capital Assets, Net of Depreciation
(in thousands of dollars)

	2003	2002
Land	$ 3,615	$ 3,615
Land improvements and infrastructure	100	-
Buildings	16,609	-
Equipment	29	38
Projects in progress	382	13,257
Total	$ 20,735	$ 16,910

- Buildings increased and projects in progress decreased due to the completion of the Horse Science Center and the Miller Arena.

More detailed information about the university's and foundation's capital assets is presented in Note 6 to the financial statements.

Debt

At June 30, 2003, the university had $81,392,341.95 in debt outstanding. The table below summarizes these amounts by type of debt instrument (in thousands of dollars).

	2003	2002
TSSBA Bonds	$ 75,490	$ 75,997
TSSBA Commercial Paper	5,902	1,867
Total debt	$ 81,392	$ 77,864

The Tennessee State School Bond Authority (TSSBA) did not issue any new bonds on behalf of the university during the year; however, commercial paper was issued during the year for the following four projects: purchase of Steinway pianos for the School of Music, purchase of a new fleet of airplanes for the Aerospace Department, property acquisitions around the perimeter of the campus, and renovation of the Smith Hall Complex for student housing. TSSBA earned an "AA" bond rating for the fiscal year. More detailed information about the university's long-term liabilities is presented in Note 7 to the financial statements.

Economic Factors That Will Affect the Future

The university began receiving notifications of potential reductions in state appropriations early in the second half of the fiscal year. These reductions were realized shortly thereafter and resulted in a 5% decrease, or $4,284,400, from the original appropriations. State appropriations for the upcoming fiscal year 2003-04 have also been reduced by approximately 9% or $7,713,200.

Given the reductions in state appropriations for both fiscal years, the university has developed a budget that contains significant cuts in operating, travel, and capital outlay expenses. Salary and benefit expenses were also reduced by cutting positions across campus, both filled and unfilled. The university has taken measures to help deal with possible future reductions in appropriations.

Across the board fee increases have been approved by the Tennessee Board of Regents, which has increased student fees by 14%.

Requests for Information

This financial report is designed to provide a general overview of the institution's finances for all those with an interest in the university's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be directed to Alan Thomas, Controller, CAB 105, Middle Tennessee State University, 1301 East Main Street, Murfreesboro, Tennessee 37132.

TENNESSEE BOARD OF REGENTS
MIDDLE TENNESSEE STATE UNIVERSITY
STATEMENTS OF NET ASSETS
JUNE 30, 2003, AND JUNE 30, 2002

	June 30, 2003	June 30, 2002
ASSETS		
Current assets:		
Cash and cash equivalents (Notes 2 and 3)	$ 37,369,963.77	$ 35,038,192.63
Short-term investments (Note 4)	20,107,679.91	18,004,475.08
Accounts, notes, and grants receivable (net) (Note 5)	9,324,787.95	9,529,796.75
Inventories (at lower of cost or market)	2,476,787.57	2,702,891.96
Prepaid expenses and deferred charges	730,102.34	256,363.58
Accrued interest receivable	52,806.31	80,236.19
Total current assets	70,062,127.85	65,611,956.19
Noncurrent assets:		
Cash and cash equivalents (Notes 2 and 3)	22,357,293.61	23,863,104.85
Investments (Note 4)	697,319.67	657,880.41
Accounts, notes, and grants receivable (net) (Note 5)	2,788,634.82	2,777,376.26
Capital assets (net) (Note 6)	191,362,345.94	182,611,574.32
Total noncurrent assets	217,205,594.04	209,909,935.84
Total assets	287,267,721.89	275,521,892.03
LIABILITIES		
Current liabilities:		
Accounts payable	1,982,611.39	2,017,414.28
Accrued liabilities	12,259,146.06	11,104,457.94
Student deposits	949,351.30	892,632.81
Deferred revenue	3,925,801.95	3,651,554.27
Compensated absences (Note 7)	1,051,274.65	1,668,834.24
Accrued interest payable	681,890.06	698,974.42
Long-term liabilities, current portion (Note 7)	2,522,927.44	2,390,069.35
Deposits held in custody for others	51,642,150.28	46,816,269.02
Other liabilities	195,022.37	99,651.53
Total current liabilities	75,210,175.50	69,339,857.86
Noncurrent liabilities:		
Compensated absences (Note 7)	3,003,574.85	2,119,002.75
Long-term liabilities (Note 7)	78,869,414.51	75,474,018.42
Due to grantors (Note 7)	3,005,097.53	3,282,034.74
Total noncurrent liabilities	84,878,086.89	80,875,055.91
Total liabilities	160,088,262.39	150,214,913.77
NET ASSETS		
Invested in capital assets, net of related debt	89,234,837.03	87,837,574.10
Restricted for:		
Nonexpendable:		
Scholarships and fellowships	10,900.00	10,900.00
Other	704,747.30	614,899.93
Expendable:		
Scholarships and fellowships	36,872.15	59,177.92
Research	271,768.66	139,235.99
Instructional department uses	68,541.09	87,514.73
Loans	1,686,827.12	1,640,845.51
Capital projects	1,390,919.24	3,256,320.62
Debt service	1,360,799.66	908,158.61
Other	769,857.43	779,390.67
Unrestricted (Note 8)	31,643,389.82	29,972,960.18
Total net assets	$ 127,179,459.50	$ 125,306,978.26

The notes to the financial statements are an integral part of this statement.

Exhibit B

TENNESSEE BOARD OF REGENTS
MIDDLE TENNESSEE STATE UNIVERSITY
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2003, AND JUNE 30, 2002

	Year Ended June 30, 2003	Year Ended June 30, 2002
REVENUES		
Operating revenues:		
Student tuition and fees (net of scholarship allowances of $12,391,421.11 for the year ended June 30, 2003, and $11,966,041.32 for the year ended June 30, 2002)	$ 65,043,588.14	$ 57,385,162.99
Governmental grants and contracts	22,414,057.25	18,026,318.29
Nongovernmental grants and contracts	627,451.29	606,037.19
Sales and services of educational departments	5,245,450.63	4,572,127.19
Auxiliary enterprises:		
Residential life (net of scholarship allowances of $1,703,820.40 for the year ended June 30, 2003; all residential life revenues are used as security for revenue bonds; see Note 7)	8,883,196.20	10,635,144.14
Bookstore (net of scholarship allowances of $1,394,034.88 for the year ended June 30, 2003; all bookstore revenues are used as security for revenue bonds; see Note 7)	7,083,866.49	8,187,911.61
Food service	530,126.77	475,246.47
Wellness facility (all wellness facility revenues are used as security for revenue bonds; see Note 7)	1,810,471.86	1,256,838.37
Other auxiliaries	3,990,830.05	3,072,368.11
Interest earned on loans to students	99,081.07	101,509.15
Other operating revenues	611,770.18	301,023.75
Total operating revenues	116,339,889.93	104,619,687.26
EXPENSES		
Operating expenses (Note 16):		
Salaries and wages	100,948,724.09	95,356,489.53
Benefits	26,689,905.88	23,191,166.09
Utilities, supplies, and other services	52,594,026.72	50,069,851.87
Scholarships and fellowships	10,437,455.35	10,871,191.29
Depreciation expense	9,758,807.72	10,094,640.50
Total operating expenses	200,428,919.76	189,583,339.28
Operating loss	(84,089,029.83)	(84,963,652.02)
NONOPERATING REVENUES (EXPENSES)		
State appropriations	83,208,100.00	79,049,100.00
Gifts	929,155.27	901,142.70
Investment income (net of investment expense of $73,728.87 for the year ended June 30, 2003, and $527,095.16 for the year ended June 30, 2002)	1,715,902.70	1,623,221.14
Interest on capital asset-related debt	(4,165,982.47)	(3,926,514.41)
Other nonoperating revenues (expenses)	569,383.04	814,275.35
Net nonoperating revenues	82,256,558.54	78,461,224.78
Loss before other revenues, expenses, gains, or losses	(1,832,471.29)	(6,502,427.24)

Exhibit B (Cont.)

TENNESSEE BOARD OF REGENTS
MIDDLE TENNESSEE STATE UNIVERSITY
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2003, AND JUNE 30, 2002

	Year Ended June 30, 2003	Year Ended June 30, 2002
Capital appropriations	1,371,984.95	3,642,168.62
Capital grants and gifts	2,385,156.27	3,469,196.77
Other	(52,188.69)	-
Total other revenues	3,704,952.53	7,111,365.39
Increase in net assets	1,872,481.24	608,938.15
NET ASSETS		
Net assets - beginning of year (Note 17)	125,306,978.26	256,372,816.82
Cumulative effects of changes in accounting principle (Note 12)		
Adoption of capitalization criteria for buildings and additions	-	(2,234,914.27)
Adoption of depreciation for capital assets	-	(127,466,383.88)
Deferred revenue recognition	-	799,665.81
Other	-	(2,773,144.37)
Net assets - beginning of year, as restated	125,306,978.26	124,698,040.11
Net assets - end of year	$ 127,179,459.50	$ 125,306,978.26

The notes to the financial statements are an integral part of this statement.

Exhibit C

TENNESSEE BOARD OF REGENTS
MIDDLE TENNESSEE STATE UNIVERSITY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2003, AND JUNE 30, 2002

	Year Ended June 30, 2003	Year Ended June 30, 2002
CASH FLOWS FROM OPERATING ACTIVITIES		
Tuition and fees	$ 65,201,861.09	$ 58,937,540.43
Grants and contracts	22,673,635.27	18,206,771.92
Sales and services of educational activities	5,255,817.62	4,557,156.04
Payments to suppliers and vendors	(52,612,370.12)	(49,689,905.98)
Payments to employees	(101,228,414.24)	(92,453,015.70)
Payments for benefits	(24,917,519.83)	(22,459,781.06)
Payments for scholarships and fellowships	(10,437,455.35)	(10,871,191.29)
Loans issued to students and employees	(261,746.75)	-
Collection of loans from students and employees	338,483.29	-
Interest earned on loans to students	102,971.77	101,302.16
Auxiliary enterprise charges:		
Residence halls	8,873,249.48	10,675,289.34
Bookstore	7,450,550.97	7,795,352.44
Food services	489,587.63	504,418.88
Wellness facility	1,810,471.86	1,256,838.37
Other auxiliaries	3,980,982.17	3,081,994.42
Other receipts (payments)	611,770.18	301,023.75
Net cash used by operating activities	(72,668,124.96)	(70,056,206.28)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	83,580,400.00	78,250,300.00
Gifts and grants received for other than capital or endowment purposes	858,345.67	868,287.86
Federal student loan receipts	49,697,262.36	136,707.54
Federal student loan disbursements	(49,623,102.27)	(154,773.86)
Changes in deposits held for others	(1,613,210.41)	(1,447,191.02)
Other noncapital financing receipts (payments)	569,383.04	-
Net cash provided by noncapital financing activities	83,469,078.39	77,653,330.52
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from capital debt	6,431,620.90	13,035,264.76
Capital - state appropriations	1,371,984.95	3,642,168.62
Capital grants and gifts received	202,944.36	3,463,296.77
Purchases of capital assets and construction	(12,571,907.61)	(11,508,395.79)
Principal paid on capital debt and lease	(2,903,366.72)	(9,760,455.47)
Interest paid on capital debt and lease	(4,190,230.17)	(3,927,751.66)
Deposit with trustee	-	(1,735,100.84)
Other capital and related financing receipts (payments)	-	823,817.22
Net cash used by capital and related financing activities	(11,658,954.29)	(5,967,156.39)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	12,000.00	66,449.43
Income on investments	1,723,960.76	1,691,127.32
Purchases of investments	(52,000.00)	(91,500.00)
Net cash provided by investing activities	1,683,960.76	1,666,076.75

TENNESSEE BOARD OF REGENTS
MIDDLE TENNESSEE STATE UNIVERSITY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2003, AND JUNE 30, 2002

	Year Ended June 30, 2003	Year Ended June 30, 2002
Net increase in cash and cash equivalents	825,959.90	3,296,044.60
Cash and cash equivalents - beginning of year	58,901,297.48	55,605,252.88
Cash and cash equivalents - end of year	$ 59,727,257.38	$ 58,901,297.48
Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	$ (84,089,029.83)	$ (84,963,652.02)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation expense	9,758,807.72	10,094,640.50
Other adjustment	(63,070.57)	-
Change in assets and liabilities:		
Receivables, net	(344,455.19)	(735,107.07)
Inventories	226,104.39	(305,103.10)
Prepaid/deferred items	(298,738.76)	90,516.18
Other assets	3,890.70	(206.99)
Accounts payable	731,162.78	(718,575.69)
Accrued liabilities	1,161,851.46	3,321,586.28
Deferred revenue	274,247.68	1,917,804.29
Deposits	56,718.49	152,901.82
Compensated absences	267,012.51	338,105.56
Due to grantors	(371,260.64)	750,883.96
Loans to students and employees	(76,736.54)	-
Other	95,370.84	-
Net cash used by operating activities	$ (72,668,124.96)	$ (70,056,206.28)
Non-cash transactions		
In-kind gifts, equipment	$ 2,182,211.91	$ -
Unrealized gains on investments	$ 11,917.25	$ -

The notes to the financial statements are an integral part of this statement.

Tennessee Board of Regents
Middle Tennessee State University
Notes to the Financial Statements
June 30, 2003, and June 30, 2002

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The university is a part of the State University and Community College System of Tennessee (Tennessee Board of Regents). This system is a component unit of the State of Tennessee because the state appoints a majority of the system's governing body and provides financial support; the system is discretely presented in the *Tennessee Comprehensive Annual Financial Report*.

Basis of Presentation

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). In June 1999, the GASB issued Statement 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*. This was followed in November 1999 by GASB Statement 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*. The financial presentation required by those statements provides a comprehensive, entity-wide perspective of the university's assets, liabilities, net assets, revenues, expenses, changes in net assets, and cash flows, and replaces the fund-group perspective previously required.

Significant accounting changes made in order to comply with the new requirements include (1) adoption of depreciation on capital assets and (2) reporting summer school revenues and expenses between fiscal years rather than in one fiscal year.

Basis of Accounting

For financial statement purposes, the university is considered a special-purpose government engaged only in business-type activities. Accordingly, the financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. All significant interfund transactions have been eliminated.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards

Board. The university has the option of following private-sector guidance issued subsequent to November 30, 1989, subject to the above limitation. The university has elected not to follow private-sector guidance issued subsequent to November 30, 1989.

Amounts reported as operating revenues include (1) tuition and fees, net of waivers and discounts; (2) federal, state, local, and private grants and contracts; (3) sales and services of auxiliary enterprises; and (4) other sources of revenue. Operating expenses for the university include (1) salaries and wages; (2) employee benefits; (3) scholarships and fellowships; (4) depreciation; and (5) utilities, supplies, and other services.

All other activity is nonoperating in nature and includes (1) state appropriations for operations; (2) investment income; (3) bond issuance costs; (4) interest on capital asset-related debt; and (5) gifts.

When both restricted and unrestricted resources are available for use, generally it is the university's policy to use the restricted resources first.

Inventories

Inventories are valued at the lower of cost or market. Textbooks included in the inventory are recorded on a first-in, first out basis. All other items are maintained on an average cost or first-in, first-out basis.

Compensated Absences

The university's employees accrue annual leave at varying rates, depending on length of service or classification. Some employees also earn compensatory time. The amount of these liabilities and their related benefits are reported in the statement of net assets.

Capital Assets

Capital assets, which include property, plant, equipment, and library holdings, are reported in the statement of net assets at historical cost or at fair value at date of donation, less accumulated depreciation. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend the asset's useful life are not capitalized.

A capitalization threshold of $100,000 is used for buildings, and $50,000 is used for infrastructure. Equipment is capitalized when the unit acquisition cost is $5,000 or greater. The capitalization threshold for additions and improvements to buildings and land is set at $50,000.

These assets, with the exception of land, are depreciated using the straight-line method over the estimated useful lives, which range from 5 to 40 years.

Middle Tennessee State University Foundation

The university is the sole beneficiary of the Middle Tennessee State University Foundation. A board independent of the university controls this private, nonprofit foundation. The university handles the financial records, investments, and other financial transactions, and the assets and liabilities of the foundation are included on the university's statement of net assets.

Net Assets

The university's net assets are classified as follows:

Invested in capital assets, net of related debt – This represents the university's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Nonexpendable restricted net assets – Nonexpendable restricted net assets consist of endowment and similar type funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may be expendable or added to principal.

Expendable restricted net assets – Expendable restricted net assets include resources which the university is legally or contractually obligated to spend in accordance with restrictions imposed by external third parties.

Unrestricted net assets – Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, and sales and services of educational departments and auxiliary enterprises. These resources are used for transactions relating to the educational and general operations of the university, and may be used at the discretion of the university to meet current expenses for any purpose. The auxiliary enterprises are substantially self-supporting activities that provide services for students, faculty, and staff.

Scholarship Discounts and Allowances

Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the statement of revenues, expenses, and changes in net assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the university and the amount that is paid by the student and/or third parties making payments on the student's behalf. Certain governmental grants, such as Pell grants, and other federal, state, or nongovernmental programs, are recorded as either operating or nonoperating revenues in the university's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, the university has recorded a scholarship discount and allowance.

NOTE 2. CASH AND CASH EQUIVALENTS

In addition to demand deposits and petty cash on hand, this classification includes instruments which are readily convertible to known amounts of cash and which have original maturities of three months or less. At June 30, 2003, cash and cash equivalents consisted of $18,743,488.76 in bank accounts, $115,115.00 of petty cash on hand, $35,989,463.96 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, $3,371,395.32 in LGIP deposits for capital projects, and $1,507,794.34 in money market accounts. At June 30, 2002, cash and cash equivalents consisted of $4,503,094.94 in bank accounts, $117,093.00 of petty cash on hand, $45,896,560.71 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, $5,941,172.82 in LGIP deposits for capital projects, and $2,443,376.01 in money market accounts.

LGIP deposits for capital projects - Payments related to the university's capital projects are made by the State of Tennessee's Department of Finance and Administration. The university's estimated local share of the cost of each project is held in a separate Local Government Investment Pool (LGIP) account. As expenses are incurred, funds are withdrawn from the LGIP account by the Tennessee Board of Regents and transferred to the Department of Finance and Administration. The funds in the account are not available to the university for any other purpose until the project is completed and the Tennessee Board of Regents releases any remaining funds.

NOTE 3. DEPOSITS

The university's deposits are in financial institutions that participate in the bank collateral pool administered by the State Treasurer. The securities pledged to protect these accounts are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public fund accounts covered by the pool are considered to be insured for purposes of credit risk disclosure.

At June 30, 2003, the carrying amount of the university's deposits was $20,251,283.10, and the bank balance was $21,756,953.36. The bank balance was insured. At June 30, 2002, the carrying amount of the university's deposits was $6,946,470.95, and the bank balance was $8,900,879.59. The bank balance was insured.

The laws of the State of Tennessee require that collateral be pledged to secure all uninsured deposits. Tennessee Board of Regents policies require that the market value of collateral pledged equal 115%, 100%, or 90% of the uninsured deposits at financial institutions participating in the collateral pool. The pledge level is based on financial criteria set by the Collateral Pool Board with the financially strongest institutions being eligible for the lowest pledge level.

The university also has deposits in the Local Government Investment Pool (LGIP) administered by the State Treasurer. The LGIP is part of the Pooled Investment Fund. The fund's investment policy and custodial credit risk are presented in the *Tennessee Comprehensive Annual Financial Report.* That report may be obtained by writing to the Tennesee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Eighth Avenue North, Nashville, Tennessee 37243-0298, or by calling (615) 741-2140.

NOTE 4. INVESTMENTS

The university is authorized by statute to invest funds in accordance with Tennessee Board of Regents policies. Under the current policy, funds other than endowments may be invested only in obligations of the United States or its agencies backed by the full faith and credit of the United States; repurchase agreements for United States securities; certificates of deposit in banks and savings and loan associations; bankers' acceptances; commercial paper; money market mutual funds; and the State of Tennessee Local Government Investment Pool. The policy requires that investments of endowments in equity securities be limited to funds from private gifts or other sources external to the university and that endowment investments be prudently diversified. The Middle Tennessee State University Foundation is authorized to invest funds in accordance with its board of directors' policies.

All investments permitted to be reported at fair value under GASB Statement 31 are reported at fair value, including those with a maturity date of one year or less at the time of purchase.

The foundation's investments are categorized below to indicate the level of risk assumed by the foundation at year-end. Category 2 consists of uninsured and unregistered investments for which the securities are held by the counterparties' trust department or agent in the foundation's name.

	June 30, 2003	June 30, 2002
Category 2:		
U.S. government securities	$ 339,778.87	$ 296,852.43
Corporate stocks	11,186,087.74	8,919,352.04
Corporate bonds	8,541,019.80	8,747,082.89
Investments not susceptible to credit risk categorization:		
Mutual funds	738,113.17	699,068.13
Total	$20,804,999.58	$18,662,355.49

Investments of the university's endowment and similar funds are composed of the following:

	Carrying Value June 30, 2003	Carrying Value June 30, 2002
Mutual funds	$ 697,319.67	$ 657,880.41

Assets of endowments are pooled on a fair value basis, with each individual fund subscribing to or disposing of units on the basis of the fair value per unit at the beginning of the calendar quarter within which the transaction takes place. The 133,495.67 units at June 30, 2003, each having a fair value of $5.22, were owned by quasi-endowments. The 130,008.658 units at June 30, 2002, each having a fair value of $5.06, were owned by quasi-endowments.

The following tabulations summarize changes in relationships between cost and fair values of the pooled assets:

FY 2003

	Pooled Assets		Net Gains	Fair Value
	Fair Value	Cost	(Losses)	Per Unit
End of year	$ 697,319.67	$ 747,188.07	$ (49,868.40)	$ 5.22
Beginning of year	$ 657,880.41	$ 719,666.06	(61,785.65)	5.06
				$ 0.16
Unrealized net gains			11,917.25	
Realized net losses			(2,746.45)	
Total net gains			$ 9,170.80	

The average annual earnings per unit, exclusive of net gains, were $0.14 for the year.

FY 2002

	Pooled Assets		Net Gains	Fair Value
	Fair Value	Cost	(Losses)	Per Unit
End of year	$ 657,880.41	$ 719,666.06	$ (61,785.65)	$ 5.06
Beginning of year	$ 653,194.02	$ 710,641.16	(57,447.14)	4.94
				$ 0.12
Unrealized net losses			(4,338.51)	
Realized net losses			(14,925.24)	
Total net losses			$ (19,263.75)	

The average annual earnings per unit, exclusive of net gains, were $0.12 for the year.

Investments of the foundation's endowment and similar funds are composed of the following:

	Carrying Value June 30, 2003	Carrying Value June 30, 2002
Mutual funds	$ 40,793.50	$ 41,187.72

Assets of endowments are pooled on a fair value basis, with each individual fund subscribing to or disposing of units on the basis of the fair value per unit at the beginning of the calendar quarter within which the transaction takes place. The 4,029.743 units at June 30, 2003, each having a fair value of $10.12, were owned by quasi-endowments. The 4,029.743 units at June 30, 2002, each having a fair value of $10.22, were owned by quasi-endowments.

The following tabulations summarize changes in relationships between cost and fair values of the pooled assets:

FY 2003

	Pooled Assets		Net Gains	Fair Value
	Fair Value	Cost	(Losses)	Per Unit
End of year	$ 40,793.50	$ 48,608.60	$ (7,815.10)	$10.12
Beginning of year	$ 41,187.72	$ 48,608.60	(7,420.88)	10.22
				$(0.10)
Unrealized net losses			(394.22)	
Realized net gains			-	
Total net losses			$ (394.22)	

There were no average annual earnings per unit, exclusive of net gains, for the year.

FY 2002

	Pooled Assets		Net Gains	Fair Value
	Fair Value	Cost	(Losses)	Per Unit
End of year	$ 41,187.72	$ 48,608.60	$ (7,420.88)	$ 10.22
Beginning of year	$ 45,710.13	$ 48,608.60	(2,898.47)	11.34
				$ (1.12)
Unrealized net losses			(4,522.41)	
Realized net gains			-	
Total net losses			$ (4,522.41)	

There were no average annual earnings per unit, exclusive of net gains for the year.

NOTE 5. RECEIVABLES

Receivables included the following:

	June 30, 2003	June 30, 2002
Student accounts receivable	$ 3,413,488.81	$ 3,055,031.66
Grants receivable	3,697,878.51	3,506,642.43
Notes receivable	488,685.25	563,983.37
Pledges receivable	747,000.00	1,247,000.00
State appropriation receivable	426,500.00	-
Other receivables	2,268,342.68	2,526,831.64
Subtotal	11,041,895.25	10,899,489.10
Less allowance for doubtful accounts	1,717,107.30	1,369,692.35
Total receivables	$ 9,324,787.95	$ 9,529,796.75

Pledges receivable are promises of private donations that are reported as accounts receivable and revenue. At June 30, 2003, and June 30, 2002, all were considered to be collectible.

Federal Perkins Loan Program funds included the following:

	June 30, 2003	June 30, 2002
Perkins loans receivable	$ 3,679,943.44	$ 3,699,809.23
Less allowance for doubtful accounts	891,308.62	922,432.97
Total	$ 2,788,634.82	$ 2,777,376.26

NOTE 6. CAPITAL ASSETS

Capital asset activity for the university for the year ended June 30, 2003, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 4,449,224.51	$ 78,000.00	$ -	$ -	$ 4,527,224.51
Land improvements and infrastructure	25,320,600.52	197,925.80	-	-	25,518,526.32
Buildings	196,375,217.92	-	1,146,773.07	31,576.01	197,490,414.98
Equipment	28,960,113.47	5,522,097.62	-	841,744.81	33,640,466.28
Library holdings	14,690,716.33	2,156,377.63	-	1,226,167.73	15,620,926.23
Projects in progress	1,891,394.70	6,968,288.48	(1,146,773.07)	17,606.00	7,695,304.11
Total	271,687,267.45	14,922,689.53	-	2,117,094.55	284,492,862.43
Less accum. depreciation:					
Land improvements and infrastructure	11,178,519.99	1,145,128.24	-	-	12,323,648.23
Buildings	68,188,988.16	4,852,009.65	-	-	73,040,997.81
Equipment	19,778,581.52	2,076,960.42	-	652,562.12	21,202,979.82
Library holdings	6,839,515.91	1,684,709.41	-	1,226,167.73	7,298,057.59
Total accum. depreciation	105,985,605.58	9,758,807.72	-	1,878,729.85	113,865,683.45
Capital assets, net	$165,701,661.87	$5,163,881.81	$ -	$ 238,364.70	$170,627,178.98

Capital asset activity for the university for the year ended June 30, 2002, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 3,787,039.61	$ 662,184.90	$ -	$ -	$ 4,449,224.51
Land improvements and infrastructure	24,685,136.68	-	1,615,906.08	980,442.24	25,320,600.52
Buildings	191,505,679.92	3,162,450.00	2,613,816.38	906,728.38	196,375,217.92
Equipment	28,844,033.34	2,258,977.00	-	2,142,896.87	28,960,113.47
Library holdings	13,995,011.59	2,065,839.33	-	1,370,134.59	14,690,716.33
Projects in progress	2,756,272.60	3,364,844.56	(4,229,722.46)	-	1,891,394.70
Total	265,573,173.74	11,514,295.79	-	5,400,202.08	271,687,267.45

Less accum. depreciation:					
Land improvements and infrastructure	9,942,385.80	1,236,134.19	-	-	11,178,519.99
Buildings	63,531,264.09	4,826,912.54	-	169,188.47	68,188,988.16
Equipment	17,366,706.42	2,425,508.67	-	13,633.57	19,778,581.52
Library holdings	6,603,565.40	1,606,085.10	-	1,370,134.59	6,839,515.91
Total accum. depreciation	97,443,921.71	10,094,640.50	-	1,552,956.63	105,985,605.58
Capital assets, net	$168,129,252.03	$1,419,655.29	$ -	$3,847,245.45	$165,701,661.87

Capital asset activity for the foundation for the year ended June 30, 2003, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 3,615,346.20	$ -	$ -	$ -	$ 3,615,346.20
Land improvements and infrastructure	-	105,019.41	-	-	105,019.41
Buildings	-	-	17,034,396.34	-	17,034,396.34
Equipment	204,020.00	545,917.60	-	698,824.60	51,113.00
Projects in progress	13,257,105.61	4,159,095.23	(17,034,396.34)	-	381,804.50
Total	17,076,471.81	4,810,032.24	-	698,824.60	21,187,679.45
Less accum. depreciation:					
Land improvements and infrastructure	-	5,250.97	-	-	5,250.97
Buildings	-	425,859.91	-	-	425,859.91
Equipment	166,559.36	7,749.25	-	152,907.00	21,401.61
Total accum. depreciation	166,559.36	438,860.13	-	152,907.00	452,512.49
Capital assets, net	$16,909,912.45	$4,371,172.11	$ -	$545,917.60	$20,735,166.96

Capital asset activity for the foundation for the year ended June 30, 2002, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$3,669,146.20	$ -	$ -	$ 53,800.00	$ 3,615,346.20
Equipment	194,020.00	15,900.00	-	5,900.00	204,020.00
Livestock	238,672.00	-	-	238,672.00	-
Construction in progress	1,561,012.55	11,696,093.06	-	-	13,257,105.61
Total	5,662,850.75	11,711,993.06	-	298,372.00	17,076,471.81
Less accum. depreciation:					
Equipment	159,533.33	7,026.03	-	-	166,559.36
Capital assets, net	$5,503,317.42	$11,704,967.03	$ -	$298,372.00	$16,909,912.45

NOTE 7. LONG-TERM LIABILITIES

Long-term liabilities activity for the year ended June 30, 2003, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
Bonds	$75,996,953.82	$1,882,997.81	$2,390,069.35	$75,489,882.28	$2,522,927.44
Commercial paper	1,867,133.95	4,548,623.09	513,297.37	5,902,459.67	-
Subtotal	77,864,087.77	6,431,620.90	2,903,366.72	81,392,341.95	2,522,927.44
Other liabilities:					
Compensated absences	3,787,836.99	2,208,175.58	1,941,163.07	4,054,849.50	1,051,274.65
Due to grantors	3,282,034.74	967,477.00	1,244,414.21	3,005,097.53	-
Subtotal	7,069,871.73	3,175,652.58	3,185,577.28	7,059,947.03	1,051,274.65
Total long-term liabilities	$84,933,959.50	$9,607,273.48	$6,088,944.00	$88,452,288.98	$3,574,202.09

Long-term liabilities activity for the year ended June 30, 2002, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
Bonds	$69,547,416.50	$ 8,375,141.28	$1,925,603.96	$75,996,953.82	$2,390,069.35
Commercial paper	5,034,110.81	117,365.18	3,284,342.04	1,867,133.95	-
Subtotal	74,581,527.31	8,492,506.46	5,209,946.00	77,864,087.77	2,390,069.35
Other liabilities:					
Compensated absences	3,449,731.43	2,215,500.38	1,877,394.82	3,787,836.99	1,668,834.24
Due to grantors	-	3,457,034.74	175,000.00	3,282,034.74	-
Subtotal	3,449,731.43	5,672,535.12	2,052,394.82	7,069,871.73	1,668,834.24
Total long-term liabilities	$78,031,258.74	$14,165,041.58	$7,262,340.82	$84,933,959.50	$4,058,903.59

Bonds Payable

Bond issues, with interest rates ranging from 3.65% to 7.75% for Tennessee State School Bond Authority bonds are due serially to 2030 and are secured by pledges of the facilities' revenues to which they relate and certain other revenues and fees of the university, including state appropriations. The bonded indebtedness with the Tennessee State School Bond Authority reported on the statement of net assets is shown net of assets held by the authority in the debt service reserve and unexpended debt proceeds. The reserve amount was $907,739.11 at June 30, 2003, and June 30, 2002. Unexpended debt proceeds were $262,115.04 at June 30, 2003, and $2,145,112.85 at June 30, 2002.

Debt service requirements to maturity for bonds payable at June 30, 2003, are as follows:

Year Ending June 30	Principal	Interest	Total
2004	$ 2,522,927.44	$ 4,016,615.75	$ 6,539,543.19
2005	2,418,430.01	3,896,899.10	6,315,329.11
2006	2,446,690.06	3,780,741.54	6,227,431.60
2007	2,570,342.09	3,662,031.22	6,232,373.31
2008	2,695,931.48	3,542,689.74	6,238,621.22
2009-2013	14,591,741.66	15,648,759.76	30,240,501.42
2014-2018	16,659,187.51	11,659,972.28	28,319,159.79
2019-2023	15,312,853.93	7,304,959.86	22,617,813.79
2004-2028	14,716,482.03	2,995,730.42	17,712,212.45
2029-2030	1,555,296.07	132,466.06	1,687,762.13
	$75,489,882.28	$56,640,865.73	$132,130,748.01

Commercial paper

The Tennessee State School Bond Authority also authorized the issuance of commercial paper to finance the costs of various capital projects. The amount issued for projects at the university was $5,902,459.67 at June 30, 2003, and $1,867,133.95 at June 30, 2002.

For the commercial paper program, the Tennessee State School Bond Authority maintains an interest rate reserve fund. The university contributes amounts to the reserve fund based on the amounts drawn. The principal of the reserve will be contributed to pay off notes or credited back to the university when the notes are converted to bonds. The interest earned on the reserve is used to pay interest due during the month.

NOTE 8. UNRESTRICTED NET ASSETS

Unrestricted net assets include funds that have been designated or reserved for specific purposes. The unrestricted net assets are composed of the following:

	June 30, 2003	June 30, 2002
Working capital	$ 2,034,843.43	$ 2,147,991.99
Encumbrances	1,907,654.99	1,649,730.86

Designated fees	288,841.01	438,769.97
Auxiliaries	4,021,406.62	4,004,895.82
Quasi-endowment	155,100.00	155,100.00
Plant construction	6,881,741.34	6,346,886.34
Renewal and replacement of equipment	12,271,270.77	12,477,731.47
Debt retirement	799,267.88	837,408.27
Unreserved/undesignated	3,283,263.78	1,914,445.46
Total	$31,643,389.82	$29,972,960.18

NOTE 9. ENDOWMENTS

If a donor has not provided specific instructions to the university, state law permits the university to authorize for expenditure the net appreciation (realized and unrealized) of the investments of endowment funds. When administering its power to spend net appreciation, the university is required to consider the university's long-term and short-term needs, present and anticipated financial requirements, expected total return on its investments, price-level trends, and general economic conditions. Any net appreciation spent is required to be spent for the purposes for which the endowment was established.

The university chooses to spend the investment income (including changes in the value of investments) each year. Under the spending plan established by the university, all interest earnings have been authorized for expenditure. At June 30, 2003, net appreciation of $2,474.39 is available to be spent, none of which is restricted to specific purposes. The amount is incuded in unrestricted net assets.

NOTE 10 PENSION PLAN

A. Defined Benefit Plan

Tennessee Consolidated Retirement System

Plan Description - The university contributes to the State Employees, Teachers, and Higher Education Employees Pension Plan (SETHEEPP), a cost-sharing, multiple-employer, defined benefit pension plan administered by the Tennessee Consolidated Retirement System (TCRS). TCRS provides retirement, death, and disability benefits as well as annual cost-of-living adjustments to plan members and their beneficiaries. Title 8, Chapters 34-37, *Tennessee Code Annotated*, establishes benefit provisions. State statutes are amended by the Tennessee General Assembly.

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for SETHEEPP. That report may be obtained by writing to the Tennessee Department of the Treasury, Consolidated Retirement System, 10th Floor Andrew Jackson Building, Nashville, Tennessee 37243-0230, or by calling (615) 741-8202.

Funding Policy - Plan members are noncontributory. The university is required to contribute an actuarially determined rate. The current rate is 7.29% of annual covered payroll. Contribution requirements for the university are established and may be amended by the TCRS' Board of Trustees. The university's contributions to TCRS for the years ended June 30, 2003, 2002, and 2001 were $2,571,010.23, $2,165,347.75, and $2,107,764.38. Contributions met the requirements for each year.

B. Defined Contribution Plans

Optional Retirement Plans (ORP)

Plan Description - The university contributes to three defined contribution plans: Teachers Insurance and Annuity Association–College Retirement Equities Fund (TIAA-CREF), Aetna Life Insurance and Annuity Company, and Variable Annuity Life Insurance Company (VALIC). These plans are administered by the Tennessee Department of the Treasury. Each plan provides retirement benefits to faculty and staff who are exempt from the overtime provisions of the Fair Labor Standards Act and who waive membership in the TCRS. Benefits depend solely on amounts contributed to the plan plus investment earnings. Plan provisions are established by state statute in Title 8, Chapter 35, Part 4, *Tennessee Code Annotated.* State statutes are amended by the Tennessee General Assembly.

Funding Policy - Plan members are noncontributory. The university contributes an amount equal to 10% of the employee's base salary up to the social security wage base and 11% above the social security wage base. Contribution requirements are established and amended by state statute. The contribution made by the university to the plans was $5,343,658.17 for the year ended June 30, 2003, and $4,977,476.97 for the year ended June 30, 2002. Contributions met the requirements for each year.

NOTE 11. OTHER POST-EMPLOYMENT BENEFITS

The State of Tennessee administers a group health insurance program which provides post-employment health insurance benefits to eligible university retirees. This benefit is provided and administered by the State of Tennessee. The university assumes no liability for retiree health care programs. Information related to this plan is available at the statewide level in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Eighth Avenue North, Nashville, Tennessee 37243-0298, or by calling (615) 741-2140.

NOTE 12. CUMULATIVE EFFECTS OF CHANGES IN ACCOUNTING PRINCIPLE

During the year ended June 30, 2002, the university implemented GASB Statement 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, and GASB Statement 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*. As a result of this implementation, the university was required to make changes in certain accounting principles, specifically the (1) adoption of capitalization criteria of $100,000 and $50,000 for buildings and additions, respectively; (2) adoption of depreciation on capital assets; (3) recording of certain summer semester revenues between fiscal years rather than in the fiscal year in which the semester was predominantly conducted; (4) reclassification of the U.S. government grants refundable amount as a liability; and (5) adoption of capitalization criteria of $5,000 for livestock. The cumulative effects of these changes on net assets are shown below:

Adoption of capitalization criteria for buildings and additions	$	(2,234,914.27)
Adoption of depreciation on capital assets	$	(127,466,383.88)
Deferred revenue recognition	$	799,665.81
Reclassification of U.S. government grants refundable	$	(2,503,034.37)
Adoption of capitalization criteria for livestock	$	(270,110.00)

NOTE 13. INSURANCE-RELATED ACTIVITIES

The state purchases commercial insurance for real property losses above $5 million per year and surety bond coverage on the state's officials and employees. In the past three fiscal years, the state has had no claims filed with the commercial insurer. A designation for casualty losses in the amount of $3.271 million for incurred losses at June 30, 2003, were established in the state's general fund to provide for any property losses not covered by the commercial insurance.

At June 30, 2003, the scheduled coverage for the university was $353,275,000 for buildings and $153,389,100 for contents. At June 30, 2002, the scheduled coverage for the university was $345,598,800 for buildings and $153,539,100 for contents.

The state has set aside assets for claim settlement in an internal service fund, the Claims Award Fund. This fund services all claims for risk of loss to which the state is exposed, including general liability, automobile liability, professional malpractice, and workers' compensation. The university participates in the Claims Award Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the university based on a percentage of the university's expected loss costs, which include both experience and exposures. This charge considers recent trends in actual claims experience of the state as a whole. An actuarial valuation is performed as of fiscal year-end to determine the fund liability and premium allocation. Since the university participates in the Claims Award Fund, it is subject to the liability limitations under the provisions of the Tennessee Claims Commission Act, *Tennessee Code Annotated*, Section 9-8-101 et seq. Liability for negligence of the university for bodily injury and property damage is limited to $300,000 per person and $1,000,000 per occurrence. The limits of liability under workers' compensation are set forth in *Tennessee Code Annotated*, Section 50-6-101 et seq. Claims are paid through the state's Claims Award Fund.

The state has also set aside assets in the Employee Group Insurance Fund, an internal service fund, to provide a program of health insurance coverage for the employees of the state with the risk retained by the state. The university participates in the Employee Group Insurance Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the university based on estimates of the ultimate cost of claims that have been reported but not settled and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims.

NOTE 14. COMMITMENTS AND CONTINGENCIES

Sick Leave - The university records the cost of sick leave when paid. Generally, since sick leave (earned one day per month with unlimited accumulation) is paid only when an employee dies or is absent because of illness, injury, or related family death, there is no liability for sick leave at June 30. The dollar amount of unused sick leave was $37,344,187.29 at June 30, 2003, and $34,315,469.73 at June 30, 2002.

Operating Leases - The university has entered into various operating leases for buildings and equipment. Such leases will probably continue to be required. Expenses under operating leases for real property were $193,645.16 and for personal property were $137,998.57 for the year ended June 30, 2003. Comparative amounts for the year ended June 30, 2002, were $178,581.94 and $78,591.98. All operating leases are cancelable at the lessee's option.

Construction in Progress - At June 30, 2003, outstanding commitments under construction contracts totaled $8,271,238.80 for the Development Facility, Todd renovation, housing renovations, several building roof replacements, Keathley University Center, Honors College, life safety renovations, parking improvements, and a new observatory, which will be funded by future state capital outlay appropriations.

Litigation - The university is involved in several lawsuits, none of which are expected to have a material effect on the accompanying financial statements.

NOTE 15. CHAIRS OF EXCELLENCE

The university had $20,812,189.54 on deposit at June 30, 2003, and $20,227,808.31 on deposit at June 30, 2002, with the State Treasurer for the university's Chairs of Excellence program. These funds are held in trust by the state and are not included in the financial statements.

NOTE 16. NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS

The university's operating expenses by functional classification for the year ended June 30, 2003, are as follows:

	Natural Classification					
Functional Classification	Salaries	Benefits	Other Operating	Scholarships	Depreciation	Total
Instruction	$60,004,155.04	$14,729,404.38	$11,398,990.94	$ -	$ -	$ 86,132,550.36
Research	1,728,191.56	362,315.80	691,516.27	-	-	2,782,023.63
Public service	3,061,708.89	860,069.93	3,239,312.31	-	-	7,161,091.13
Academic support	9,358,123.97	2,647,636.64	760,517.56	-	-	12,766,278.17
Student services	9,029,689.61	2,499,638.84	8,158,952.19	-	-	19,688,280.64
Institutional support	7,908,942.01	2,468,801.38	2,595,504.43	-	-	12,973,247.82
Operation & maint.	4,823,495.53	1,717,882.69	12,564,281.76	-	-	19,105.659.98
Scholar. & fellow.	-	-	-	10,437,455.35	-	10,437,455.35
Auxiliary	5,034,417.48	1,404,156.22	13,184,951.26	-	-	19,623,524.96
Depreciation	-	-	-	-	9,758,807.72	9,758,809.72
Total	$100,948,724.09	$26,689,905.88	$52,594,026.72	$10,437,455.35	$9,758,807.72	$200,428,919.76

The university's operating expenses by functional classification for the year ended June 30, 2002, are as follows:

	Natural Classification					
Functional Classification	Salaries	Benefits	Other Operating	Scholarships	Depreciation	Total
Instruction	$56,447,943.96	$12,889,064.42	$10,325,841.47	$ 2,283,815.40	$ -	$ 81,946,665.25
Research	1,708,018.97	321,200.78	620,192.06	45,859.40	-	2,695,271.21
Public service	2,733,048.65	688,237.86	2,471,583.39	257,161.53	-	6,150,031.43
Academic support	8,637,282.59	2,269,994.48	240,842.90	87,553.41	-	11,235,673.38
Student services	8,477,153.35	2,239,676.82	7,887,583.36	3,244,343.43	-	21,848,756.96
Institutional support	7,769,151.83	2,100,682.88	2,903,496.14	83,279.91	-	12,856,610.76
Operation & maint.	4,801,871.60	1,514,211.64	13,636,385.11	10,000.00	-	19,962,468.35
Scholar. & fellow.	-	-	7,714.72	4,838,595.95	-	4,846,310.67
Auxiliary	4,782,018.58	1,168,097.21	11,976,212.72	20,582.26	-	17,946,910.77
Depreciation	-	-	-	-	10,094,640.50	10,094,640.50
Total	$95,356,489.53	$23,191,166.09	$50,069,851.87	$10,871,191.29	$10,094,640.50	$189,583,339.28

NOTE 17. PRIOR-YEAR RESTATEMENT

Due to changes in presentation made by the university for the year ended June 30, 2003, some reclassifications were made in the prior-year financial statements for comparative purposes. The LGIP deposit – capital projects was reclassified as noncurrent cash and cash equivalents. The TSSBA interest rate reserve, which was previously shown as deposit with trustee, was reclassified as prepaid expense. Also, the note disclosure for unrestricted net assets was changed to show all of the components rather than just the designated amounts. In addition, the investments note disclosure was restated to properly reflect corporate bonds of $7,471,883.79 for the foundation, which were previously reported as mutual funds.

The invested in capital assets, net of related debt at June 30, 2001, was restated to reflect the follwing prior period adjustments: (1) capitalization of stadium turf replacement not previously recorded in the amount of $492,014.86, (2) removal of glass repair totaling $84,270.00 previously capitalized, (3) removal of old telephone system in the amount of $2,109,944.10 not removed when new system was installed, and (4) removal of electronic media databases previously capitalized as library holdings for $227,314.69. The net effect was a decrease in net assets of $1,929,513.93.